Town of Amherst
Town of Pelham
Amherst-Pelham Regional School
GASB Statements No. 43 and 45

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Background

- Other Post Employment Benefit (OPEB) refers to any post employment benefit other than pensions
  - Medical
  - Long-term Care
  - Dental
  - Vision
  - Life Insurance and Disability (if not in pension plan)
- Post-employment benefits are part of the compensation for services rendered by employees; i.e., they are part of an exchange transaction
- Benefits are "earned," and obligations accrue or accumulate, during employment

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Background

- Payment is deferred until after employment
- Last deferred expense to be addressed by Governmental Accounting Standards Board (GASB)

Disclosures

- Annual Required Contribution (ARC) is the amount to be expensed for the year
  - Determined in a similar manner as the Pension Appropriation, accept it is not required to be in the budget
  - Normal Cost plus amortization of unfunded accrued liability
- Accrued Liability
- Assets – Balance Sheet and Income/Expense
- Unfunded Accrued Liability
- 10 year history
- Accumulated differences between the ARC and actual contributions creates an additional liability or asset

Actuarial Valuation – Assumptions

- Same demographic assumptions as used for Pension Valuations
- Discount rate for "Pre-funded" basis would be about 7% (represents the expected long-term return on a new trust fund)
- Discount rate for current "Pay-as-you-go" basis would be about 4.25% (represents the expected long-term return on current cash and short-term investments)
- Healthcare cost trend rates, initially about 9%, ultimate of 4% to 5%
- Expected portion of active employees electing: e.g. 80%

Disclosures – Pre-funded Approach

- Footnote Disclosures use about an 7% discount rate assumption
  - Lower accrued liability and ARC
- If you fund less than the ARC then a Net OPEB Obligation (NOO) is created and placed on the balance sheet as a liability
    - This assumes you will increase the funding to be equal to the ARC over a short period of years
    - Contingent on the auditor agreeing with approach
- The following year, you would need to adjust the NOO with interest, amortization and for any differences between the new ARC and actual contributions

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Disclosures – Pay-as-you-go Approach

- Footnote Disclosures at about 4.25% discount rate assumption
  - Much larger Unfunded accrued liability and ARC
- If you fund the Pay-as-you-go cost then a large Net OPEB Obligation (NOO) is created and placed on the balance sheet
- The following year, you would need to adjust the NOO with interest and for any differences between the new ARC and actual contributions

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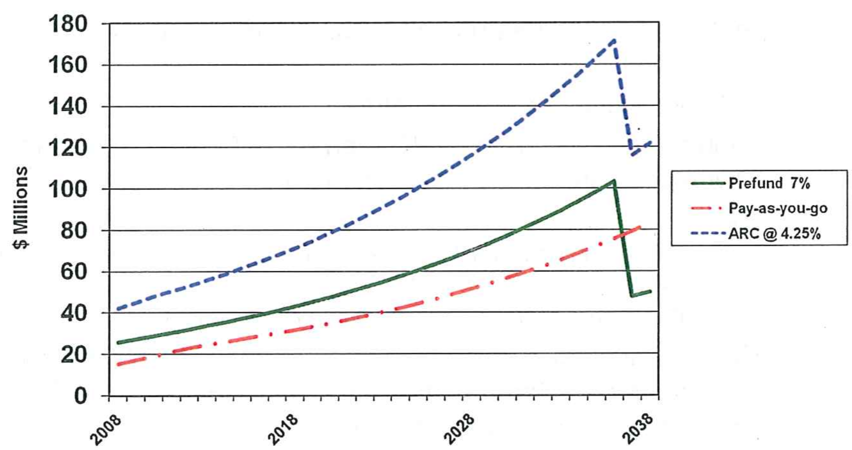
Sample ARC and Pay-as-you-go Forecast



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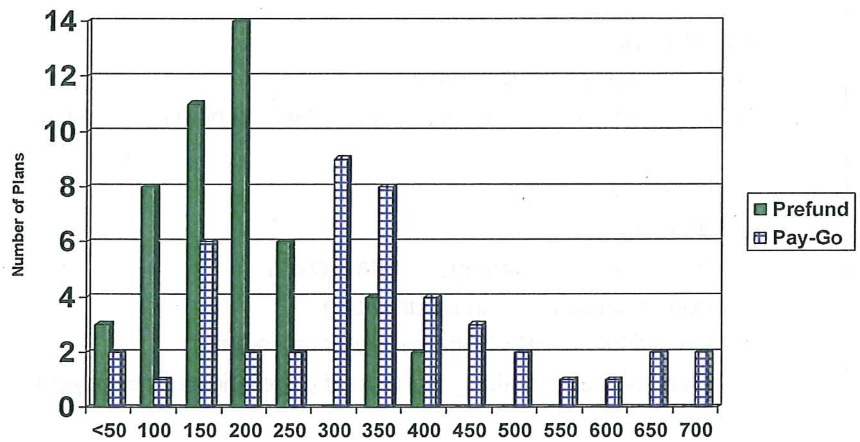
Buck Boston GASB 45 Actuarial Valuations
Unfunded Liability as a Percentage of Payroll



Prefund: 48 plans, Average = 161%

Pay-go: 45 plans, Average = 313%

As of 1/1/2010

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Pre-funding

- Advantages
  - More economical over time – investment returns will supplement employer and employee contributions
  - Increased security for employees and retirees
  - Helps maintain bond rating
  - Assists in budgeting – available assets act like a reserve to smooth large increases in medical costs
  - Keeps a new book liability under control
- Disadvantages
  - Higher short term cash outlay
  - Higher administrative costs
  - More complex

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Pay-as-you-go

- Advantages
  - Lower current cash outlay
  - No administrative costs associated with a new separate Trust Fund
  - Easier to understand
- Disadvantages
  - No investment earnings to offset costs
  - Potential reduction in credit rating
  - Large Net OPEB Obligation on balance sheet
  - Maintains cost shifting to the next generation of tax payers

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Expense and Balance Sheet Entries

- ARC is entered on the Financials (not necessarily the budget) as an expense on the Income and Expense sheets
- Actual cash contribution is a credit against the ARC
- Net OPEB Obligation (NOO) is a Balance Sheet entry

Fiscal Year Ending	Annual Required Contribution	Interest on NOO	Amortization of NOO	OPEB Cost (1)+(2)-(3)	Actual Contribution	Change in NOO (4)-(5)	NOO Balance
2009	6,820	-	-	6,820	1,431	5,389	5,389
2010	7,150	189	293	7,046	1,605	5,441	10,830
2011	7,497	379	589	7,287	1,761	5,526	16,356
2012	7,860	572	889	7,543	1,955	5,588	21,944
2013	8,241	768	1,193	7,816	2,162	5,654	27,598
2014	8,640	966	1,501	8,105	2,293	5,812	33,410
2015	9,058	1,169	1,817	8,411	2,469	5,942	39,352

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Challenges of Pre-funding

- A trust is required with provisions that the assets are used for the exclusive use of OPEB, and related expenses
- IRS rules include 3 mechanisms for establishing trusts on a tax advantaged basis
  - Voluntary Employee Benefit Association (VEBA)
  - Medical Accounts for Retirees
  - Government Trust under IRC Section 115 (Massachusetts General Law 32B Section 20)
- Increases in appropriations sufficient to justify using the higher discount rate
- If you can not raise appropriations to the ARC, a discount rate between 7% and 4.25% would be required

Challenges of Pre-funding – Section 115

- Governmental Trust is a trust that qualifies for exemption from Federal income tax under Section 115.
  - Established only for an essential government function and the income earned on the trust's investments have to accrue to the state or local government's benefit
  - Arlington, Needham, Bedford, Wellesley and many more

Prefunding – Needham's Approach

- First OPEB Study completed many years ago
- Full Prefunding would have required an increase of over $2 million in the budget, more than double current costs
- Homerule petition created a trust
- Town meeting approved an additional $300,000 to prefund, increasing annually thereafter
- Plan provisions were adjusted
- Section 20 of MGL 32B adopted
- As of July 1, 2009
  - $5 million in Trust
  - 10.2% Funded
  - Fully funding their ARC

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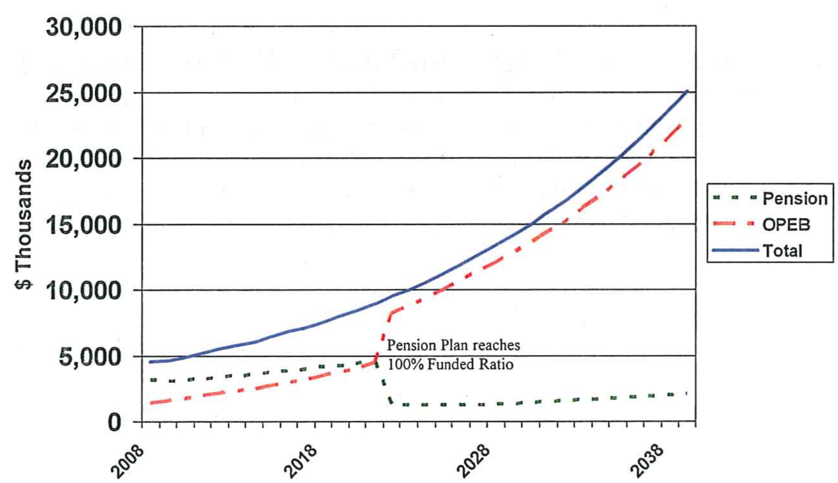
Funding Both Pension and OPEB



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Town of Amherst

		Full Pre-funding	No Pre-funding	
a)	Funding Policy	Full Pre-funding	No Pre-funding	
b)	Discount Rate	7.00%	4.25%	
c)	Actuarial valuation date	June 30, 2010	June 30, 2010	Difference
d)	Actuarial Value of Assets	$ 0	$ 0	$ 0
e)	Actuarial Accrued Liability	$ 50,824,623	$ 74,870,058	$ 24,045,435
f)	Unfunded Actuarial Liability "UAL" [e - d]	$ 50,824,623	$ 74,870,058	$ 24,045,435
g)	Funded ratio [d / e]	0.0%	0.0%	0.0%
h)	Annual covered payroll	25,788,641	25,788,641	
i)	UAL as percental of covered payroll	197.1%	290.3%	
j)	Normal Cost for fiscal year end 2010	$ 1,526,179	$ 3,043,227	$ 1,517,048
k)	Amortization of UAL for fiscal year 2010 *	$ 2,950,498	$ 3,156,033	$ 205,535
l)	Annual Required Contribution "ARC" for fiscal year 2010 [j + k]	$ 4,476,677	$ 6,199,260	$ 1,722,583
m)	Expected benefit payments	$ 1,971,851	$ 1,971,851	$ 0

* 30-year amortization, increasing 2.5% per year
** Also increase in Net OPEB Obligation (NOO)

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Town of Pelham

		Full Pre-funding	No Pre-funding	
a)	Funding Policy	Full Pre-funding	No Pre-funding	
b)	Discount Rate	7.0%	4.25%	
c)	Actuarial valuation date	June 30, 2010	June 30, 2010	Difference
d)	Actuarial Value of Assets	$ 0	$ 0	$ 0
e)	Actuarial Accrued Liability	$ 2,773,509	$ 4,043,473	$ 1,269,964
f)	Unfunded Actuarial Liability "UAL" [e - d]	$ 2,773,509	$ 4,043,473	$ 1,269,964
g)	Funded ratio [d / e]	0.0%	0.0%	0.0%
h)	Annual covered payroll	1,094,376	1,094,376	
i)	UAL as percental of covered payroll	253.4%	369.5%	
j)	Normal Cost for fiscal year end 2010	$ 77,661	$ 147,568	$ 69,907
k)	Amortization of UAL for fiscal year 2010 *	$ 161,009	$ 170,446	$ 9,437
m)	Annual Required Contribution "ARC" for fiscal year 2010 [j + k]	$ 238,670	$ 318,014	$ 79,344
n)	Expected benefit payments	$ 92,924	$ 92,924	$ 0

* 30-year amortization, increasing 2.5% per year

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Amherst-Pelham Regional School District

		Full Pre-funding	No Pre-funding	Difference
a)	Funding Policy	Full Pre-funding	No Pre-funding	
b)	Discount Rate	7.00%	4.25%	
c)	Actuarial valuation date	June 30, 2010	June 30, 2010	Difference
d)	Actuarial Value of Assets	$ 0	$ 0	$ 0
e)	Actuarial Accrued Liability	$ 30,186,885	$ 43,356,051	$ 13,169,166
f)	Unfunded Actuarial Liability "UAL" [e - d]	$ 30,186,885	$ 43,356,051	$ 13,169,166
g)	Funded ratio [d / e]	0.0%	0.0%	0.0%
h)	Annual covered payroll	15,801,923	15,801,923	
i)	UAL as percental of covered payroll	191.0%	274.4%	
j)	Normal Cost for fiscal year end 2010	$ 857,549	$ 1,657,042	$ 799,493
k)	Amortization of UAL for fiscal year 2010 *	$ 1,752,425	$ 1,827,608	$ 75,183
l)	Annual Required Contribution "ARC" for fiscal year 2010 [j + k]	$ 2,609,974	$ 3,484,650	$ 874,676
m)	Expected benefit payments	$ 1,463,160	$ 1,463,160	$ 0

* 30-year amortization, increasing 2.5% per year

Potential Plan Changes

- Increases in retiree co-share
- Increases in deductibles and co-pays
- Restricted availability
  - Must retire from the town with at least X years of service
  - If less than Y years of service with town, then a higher co-share by the retiree
  - No or reduced spousal coverage
  - Some plans no longer treat the retiree in the exact same manner as the employee
- Measuring the change in promise under GASB 45 provides insight to the value of the modifications

Reactions across the Country

- Some States have already established trusts and are starting to pre-fund. A 2/17/06 report from California indicated 11 states have started pre-funding. For example, Ohio and Minnesota
- State of Massachusetts set aside an additional $300 million in FYE08, $0 for 2009 & 2010. Many municipalities have also established trusts and started pre-funding.
- Communities outside of Massachusetts have been more active in establishing trusts due to less restrictive state laws (e.g. Cranston, Newport, Providence, Middletown)
- City of Gainesville issued OPEB bonds
- Benefit studies seeking to reduce the obligation, or at least keep it from rising as rapidly as in the past via multi-tiered plans
- Many are planning to shift the reductions in pension appropriations to OPEB when the pension plan reaches full funding

Medicare: Section 18

- Adopting Section 18 of MGL Chapter 32B requires all that are eligible to join Medicare, must at age 65
- Available medical plans are restricted to supplemental plans
- Results in substantial savings
  - ARC reductions of 5% - 6% immediately, 9% - 10% long term as unfunded liability is reduced and more employees are eligible for Medicare coverage
  - Medicare supplemental plans have a history of lower annual cost increases